IN THE

Supreme Court of the United States

October Term, 1957

No. 18

ROBERT H. MCNEILL, *Petitioner*,

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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INDEX

	Page
Opinions Below	1
Jurisdiction	2
Questions Presented	2
Statutes and Regulations Involved	2
Statement of Facts	4
Argument	9
Conclusion	20
Appendix:	
Tax Court Opinion, 27 T.C. 879	1a
Tax Court Decision	15a
Opinion of Court of Appeals for the 4th Circuit	16a
Judgment of Court of Appeals for the 4th Circuit	21a
Petition for Rehearing or in the Alternative for Modification of the Mandate to Order the Court Below to Take Further Testimony	23a
Order Denying Petition for Rehearing	33a

TABLE OF CASES CITED

Ambassador, Inc. (Sept. 30, 1952) Memo. Op., Doc. 29629	14
Baumgartener v. *U. S.* (1944) 322 U. S. 665	16
Boyle, Orrin E. (Feb. 9, 1942) Memo. Op., Doc. 105503	14
Burns v. *Commissioner* (CA 4, 1955) 219 F. 2d 128	14, 20
Carter-Colton Cigar Co. (1947) 9 T.C. 219	15
Dougherty Co., P. 5 T.C. 791	15
Elbert, Robert J. T.C. Memo. 1957-108	21
Factoria Land Co. (Feb. 28, 1946) Memo. Op., Doc. 2702	14
Foran v. *Commissioner* (CA 5, 1948) 165 F. 2d 705	18, 19
Galena Oaks Corp. v. *Scofield* (CA 5, 1954) 218 F. 2d 217	18

Page

Gamble v. *Commissioner* (CA 5, 1957) 242 F. 2d 586 .. 17
Goldberg v. *Commissioner* (CA 5, 1951) 223 F. 2d 709 11, 12
Goodman, Julius (1939) 40 BTA 22 13
Gruver v. *Commissioner* (CA 4, 1944) 142 F. 2d 363 .. 16
Helvering v. *Nebraska Bridge Supply & Lumber Co.* (1941) 312 U.S. 666 ..... 12, 13
King v. *Commissioner* (CA 5, 1951) 189 F. 2d 122, cert. denied (1951) 16
Kittridge v. *Commissioner*, 88 F. 2d 632 15
Kruse, Albert (1957) 29 T.C. No. 51 14
Mauldin, C. E. (1951) 16 T.C. 698, aff'd (CA 10, 1952) 195 F. 2d 714 16
McCarty v. *Cripe* (CA 7, 1953) 201 F. 2d 679 13
McGah v. *Commissioner* (CA 9, 1954) 210 F. 2d 769 .. 18
Morley, Walter G. (1947) 8 T.C. 904 14
Payer, Harry F. (Oct. 8, 1946) Memo. Op., Doc. 7701 14
Pennsylvania R.R. Co. v. *Chamberlain* (1933) 165 F. 2d 705 ..... 18, 19
Richards v. *Commissioner* (CA 9, 1936) 81 F. 2d 369 .. 16
Wener v. *Commissioner* (CA 9, 1957) 242 F. 2d 938 .. 17
White, Ethel S. (Sept. 25, 1947) Memo. Op., Doc. 12570 aff'd (CA 5, 1949) 172 F. 2d 629 14
Wright, Jr., Solomon (1947) 9 T.C. 173 15
Yellow Cab Co. of Pittsburgh v. *Driscoll* (D.C. Pa., 1938) 24 F. Supp. 993 15

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To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioner, appellant below, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in the above cause on January 11, 1958.

OPINIONS BELOW

The opinion of the Tax Court of the United States was dated March 11, 1957 and entered March 12, 1957. It is reported at 27 T.C. 899 (App. 1a).

The opinion of the United States Court of Appeals for the Fourth Circuit was filed on January 11, 1958, and is reported at 251 F. (2d) 863 (App. 16a).

JURISDICTION

The judgment of the United States Court of Appeals for the Fourth Circuit here sought to be reviewed was dated and filed on January 11, 1958. (App. 21a)

A petition for a rehearing or in the alternative for a modification of the mandate to order the court below to take further testimony was timely filed with the United States Court of Appeals for the Fourth Circuit on March 1, 1958, and denied by the Court on March 17, 1958. (App. 23a)

On June 5, 1958, an order extending the time to and including July 16, 1958 within which to file petition for writ of certiorari was entered.

The jurisdiction of this Court is invoked pursuant to the provisions of 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

I. Is the character bestowed upon real property at the time of its acquisition thereafter retained unless subsequently changed by significant acts?

II. Is it improper for a trial court to disregard the uncontradicted testimony of an otherwise impeached witness?

STATUTES INVOLVED

The pertinent statutes are as follows:

Sec. 23. *Deductions from Gross Income.*

In computing gross income there shall be allowed as deductions:

Sec. 23 (e) *Losses by Individuals.*—In the case of an individual, losses sustained during the tax-

able year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. No loss shall be allowed as a deduction under this paragraph if at the time of the filing of the return such loss has been claimed as a deduction for estate tax purposes in the estate tax return.

Sec. 117 (a) *Capital Gains and Losses.*

(a) Definitions.—As used in this chapter—

(1) Capital assets—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include—

(A) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;

(B) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in section 23(l), or real property used in his trade or business.

Sec. 117 (j) *Gains and Losses from Involuntary Conversion and from the Sale or Exchange of Certain Property Used in the Trade or Business.*—

(1) Definition of property used in the trade or business.—For the purposes of this subsection the

term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (b) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, * * *.

STATEMENT OF FACTS

Petitioner is an individual, 82 years of age, who was admitted to the Bar in 1898. He is now, and has been for over fifty years active in real estate in addition to the practice of his profession of law.

About 1916, Petitioner and two associates commenced a development known as Potomac Heights, situated on the Potomac River near Washington, D. C. As individuals they subdivided the acreage and built homes. There are presently around 300 homes in the subdivision.

Shortly thereafter petitioner purchased additional acreage in the same area, which he likewise subdivided. Lots in this development, known as Albany Park, were then sold to individual purchasers.

Several years later petitioner became active as an officer in a land company which developed a subdivision known as Spring Lake Park, located near Rockville, in Montgomery County, Maryland. This subdivision consisted of around 400 lots. The systematic selling of these lots was temporarily interrupted by

the depression. Petitioner, as an individual, still owns lots in this subdivision.

In 1924 petitioner acquired in excess of 800 acres, about ten miles from Altoona, Pennsylvania. This property was located on a plateau on Wopsononock Mountain at an elevation of about 2800 feet.

At the time he acquired this property it was his intention to make a profit by developing and selling lots. Experienced engineers were employed who surveyed the property and prepared the necessary plats showing lots which thereafter were offered for sale, both privately and at auction. In addition, petitioner expended the necessary funds to build a road through a heavy forest to the top of the plateau in order to make them accessible.

From the time of acquisition in 1924 until his equity of ownership was extinguished in 1946, petitioner made a continuous effort to develop and sell the property. In this connection, he retained an attorney experienced in real estate matters and also employed a prominent realtor, both of whom were located in that community. The realtor in turn employed various agents and salesmen. Lots were extensively advertised for sale not only in the newspapers but also by circular letters and individual letters written by petitioner and the realtor. As part of the intensive selling campaign, an elaborate auction was attempted during 1925. It had been preceded by a strenuous advertising campaign. Approximately 500 prospective purchasers were in attendance at the auction which ended in a complete failure when a sudden storm developed and the crowd dispersed.

Thereafter, as part of his continuing effort to make the area more attractive, petitioner devoted much time and activity in unsuccessful efforts to interest the Federal Government, the State of Pennsylvania and Blair County in using a portion of the land to develop a park project. Likewise a strenuous effort was made to develop an airport. In connection with these attempts petitioner personally devoted much time and effort and additionally employed agents.

Although these combined efforts eventually resulted in various commitments from the Federal and State Governments, as well as Blair County, they finally proved unsuccessful.

Meanwhile in the early 1930's petitioner had acquired acreage at Front Royal, Virginia. This land was developed and subdivided by petitioner and he still retains a substantial interest in the unsold lots remaining in this development.

In addition petitioner's activities also include the purchase, development and sale of properties in Montgomery County, Maryland, as well as individual lots in Washington, D. C.

Further petitioner has purchased acreage in various sections of North Carolina, which he thereafter developed and sold. Not heretofore mentioned is other development property located in the State of Virginia still owned by petitioner.

Further real estate activities of petitioner include the organizing and active participation in a real estate company that acquired the land and thereafter constructed the Southern Building, an office building in Washington, D. C. He was also active in financing

the Lafayette Office Building and Veterans Administration Building, as well as the Roger Smith Hotel, all in Washington, D. C., and the Congressional Country Club in Montgomery County, Maryland.

Petitioner testified unequivocally that he has been active in the real estate business each year since coming to Washington in 1903.

Petitioner was the only witness who testified at the hearing before the Tax Court and the uncontradicted testimony of this unimpeached witness was entirely consistent with the facts otherwise proved.

In 1940 the Wopsononock property previously referred to was seized by the authorities of Blair County, Pennsylvania, for unpaid real estate taxes. These authorities retained title to this property for a number of years while trying unsuccessfully to sell it. Eventually on December 5, 1946, the political subdivision holding title to the property sold it to the Royal Village Corporation and transferred title to the purchaser by deed. On this date, the statutory right of redemption which had heretofore remained in petitioner was extinguished by operation of law. See Purdon's Pennsylvania Statutes Anno. (Perm. Ed.), Secs. 5971(p), 5971(q) and 6105.1.

After 1940, despite the fact that the property had been seized by public authorities, petitioner persisted in his efforts to sell the property for the reason that so long as the right of redemption existed there still remained the possibility that he could realize a profit. These efforts by petitioner and his agents continued until the right of redemption was in fact extinguished in 1946.

On his income tax return for the taxable year 1946, petitioner deducted $11,000 as an ordinary loss resulting from the seizure and sale of the Wopsononock property.

The Statutory Notice of Deficiency issued by the Commissioner of Internal Revenue disallowed the deduction as follows:

> "The claimed deduction of $11,000 alleged to represent a loss incurred in connection with certain real estate is disallowed as not representing an allowable deduction for Federal tax purposes."

The Tax Court of the United States had jurisdiction pursuant to the provisions of 26 U.S.C. 6213 (a) and 7442.

The petitioner was the only witness to testify in the proceedings in the Tax Court. His testimony was uncontradicted and he was not otherwise impeached. On direct, cross and redirect examinations, he stated that he had been active in the real estate business for approximately 50 years; that this period of activity included not only the year 1946 in which the loss was claimed but also each of the approximate 40 years preceding and 10 years subsequent thereto; and that the scope of this real estate activity included not only the property in Pennsylvania, but simultaneously many other properties and real estate transactions all of which together formed a continuous pattern going to make up his "real estate business."

In its opinion, the Tax Court disallowed the loss as resulting from a transaction between related taxpayers and thus prohibited by Section 24(b) of the Internal Revenue Code of 1939. Although unneces-

sary to its conclusion, the Tax Court found as a fact that in 1946 the property was not held by petitioner for sale to customers in the ordinary course of his business. A further finding of the Tax Court however was that petitioner's attempts to sell the land after its seizure by officials and his offering in 1946 to satisfy the mortgage outstanding against the property demonstrated his intention to retain control over it.

The Court of Appeals held that Section 24(b) was not applicable but concluded that since the Tax Court had found that petitioner was not engaged in the real estate business that they were bound by this finding. On this basis, they reversed and remanded to the Tax Court with instructions to allow the loss within the limitations of the capital loss provisions.

ARGUMENT

I. The Character Bestowed Upon Real Property At the Time Of Its Acquisition Is Thereafter Retained Unless Subsequently Changed By Significant Acts.

The following facts found by the Tax Court contradict their determination that the Wopsononock property was a capital asset instead of an ordinary asset held by petitioner primarily for sale to customers:

> (a) Petitioner acquired the Wopsononock property with the intention to develop and subdivide the land and then sell lots to the public at auction or through separate sales transactions. (App. 2a.)
>
> (b) In this connection experienced engineers were employed to survey the property and prepare plats of the land being offered for sale. (App. 2a, 3a.)

(c) At his own expense, petitioner built a road through the forest to the top of a plateau where the lots held for sale were located. (App. 3a.)

(d) Petitioner repeatedly advertised the lots for sale; he employed a prominent realtor in the community to list the property and extensive sales efforts were made. (App. 3a.)

(e) After the failure of these efforts, petitioner further attempted to promote the sale of his land by developing an airport project within the area and also by trying to interest the State of Pennsylvania in developing a public park on the land. (App. 3a.)

(f) Following the failure of all these efforts and projects, the property was seized by county officials for taxes in 1940. (App. 3a.)

(g). Petitioner, however, continued his efforts to sell all or any part of the land since under Pennsylvania law he still retained a right of redemption. (App. 3a.)

(h) In 1946 the property was sold by the public officials and at this moment, by operation of law, petitioner's equity of redemption was extinguished. (App. 8a.)

(i) On his income tax return for the taxable year 1946, petitioner deducted as an ordinary loss the amount of $11,000 as being his basis in the property. (App. 4a.)

In its opinion the Tax Court in commenting on the extent of petitioner's activities between the time when the land was seized for taxes in 1940 and the time when

his right of redemption was lost in 1946, stated as follows: (App. 6a).

> "* * * moreover, his conduct in further attempting to sell the land after its seizure by Blair County and in offering to satisfy the mortgage outstanding against the property in May 1946, demonstrates his intention to retain control over it. * * *"

The evidentiary facts as found by the Tax Court will support no legal conclusion other than that petitioner acquired this property primarily for sale to customers. As property so held it was an ordinary asset and it is axiomatic, as stated in *Goldberg* v. *Commissioner* (CA 5, 1951), 223 F. 2d 709, that real property does not lose the character bestowed upon it at the time of its acquisition unless there is first established affirmative and significant acts to show a change of original intent.

> "* * * the original purpose is important for to counterbalance it there must be significant suggestive evidence of a change in that purpose."

Contrary to its evidentiary findings, previously set forth, the Tax Court concluded that Petitioner was neither in the real estate business nor was the property held by him primarily for sale in 1946. (App. 5a.)

The Court of Appeals found that the petitioner made diligent efforts to sell the property in the years immediately following its acquisition and was in fact in the real estate business at that time but concluded that they were bound by the finding of the Tax Court as to petitioner's status during 1946. (App. 19a, 20a.)

It is petitioner's position that having once determined that petitioner was engaged in the real estate

business and that the property was held by him primarily for sale to customers, it then becomes necessary, within the principle of the *Goldberg case, supra,* as a condition precedent to altering the character of the land from an ordinary asset to a capital asset, that there first be established some identifying event or other significant evidence justifying the change in purpose.

In the instant case, there is a complete lack of any legally significant or sufficient evidence tending to establish a change in the intent or purpose for which the land was held.

The seizure of the property for taxes by public authorities and the subsequent loss of the right of redemption is certainly not an event that *per se* converts property from an ordinary asset to a capital asset. In this respect, however, the Tax Court appears to have been misled by the Commissioner's argument as to the principle set forth by this Court in *Helvering* v. *Nebraska Bridge Supply & Lumber Co.* (1941), 312 U.S. 666. As stated by that Court, the Commissioner argued as follows: (App. 6a).

> "In the alternative, respondent asserts that if any loss is allowable it is at most a long-term capital loss arising from the sale during 1946 of a capital asset, relying upon the decision of the Supreme Court in *Helvering* v. *Nebraska Bridge Supply & Lumber Company,* 312 U.S. 666."

The Tax Court's obvious misinterpretation of the *Nebraska Bridge case, supra,* is shown by the following language from their opinion: (App. 7a).

> "* * * Accordingly, any loss resulting from the expiration of his equity of redemption of the land in question by petitioner herein is in the nature of

> a capital loss and, if allowed, is subject to the limitations of 117 (d) of the 1939 Code."

In this connection, it is petitioner's view that, correctly interpreted, *Nebraska Bridge, supra,* merely holds that a tax foreclosure and extinguishment of a right of redemption may be regarded as a "sale or exchange" for the purpose of applying Sec. 117, if the asset involved was a capital asset. If, however, the asset was not a capital asset and the loss is otherwise recognizable under some other section of the Internal Revenue Code, it is to be so allowed. See *McCarty* v. *Cripe* (CA 7, 1953) 201 F. 2d 679 wherein on facts not unlike those here involved, the Court said:

> "* * * no question is made but that the decedent lost $34,425.16, his investment in the Euclid Farm, and that it was an allowable deduction generally for uncompensated business losses."

The Tax Court's erroneous view was then compounded to petitioner's detriment by their apparent rationale that under the doctrine of *Nebraska Bridge* any loss suffered as the result of the extinguishment of a right of redemption was a capital loss. Since it was a capital loss it must result from the sale or exchange of a capital asset and therefore the property here involved must, by analysis, be a capital asset.

Nor can the fact that there were no sales of the property for several years be regarded as significant evidence suggestive of a change in the purpose for which the land was held. This is particularly so when such failure is the result of business adversity for these factors do not change the primary purpose for which property is held. *Julius Goodman* (1939) 40

BTA 22; *Walter G. Morley* (1947) 8 T.C. 904; *Orrin E. Boyle* (Feb. 9, 1942) Memo. Op., Doc. 105503; *Harry F. Payer* (Oct. 8, 1946) Memo. Op., Doc. 7701; *Factoria Land Co.* (Feb. 28, 1947) Memo. Op., Doc. 2702; *Ethel S. White* (Sept. 25, 1947) Memo. Op., Doc. 12570, aff'd (CA 5, 1949) 172 F. 2d 629; *Ambassador, Inc.* (Sept. 30, 1952) Memo. Op., Doc. 29629; *Burns* v. *Commissioner* (CA 4, 1955) 219 F. 2d 128.

In *Alfred Kruse* (1957) 29 T.C. No. 51, the Tax Court correctly states the fundamental principle that the character bestowed upon real property at the time of its acquisition is not changed by mere inactivity.

> "We think there can be no doubt that mere discontinuance of the active use of the property does not change its character previously established as business property."

In *Walter G. Morley* (1947) 8 T.C. 904, on facts parallel to those in the instant proceeding, the Court found that the taxpayer's activity was not restricted or halted by reason of any change in his plans or purposes but rather by the force of economic circumstances beyond his control. They concluded that the *character of the losses was not controlled by the absence of business activity in the year of loss:* (italics supplied)

> "There can be no question but that the business of buying and selling real estate was regularly carried on by Petitioner prior to 1931. The properties here in question were purchased or acquired by Petitioner for reselling for a profit before that date. Even though we should assume, *arguendo*, that the business of selling real estate although engaged in by Petitioner in 1940, was not one regularly carried on by him in that year, nevertheless, we would conclude that the losses in ques-

tion were attributable to a business of buying and selling real estate which was regularly carried on by him in years prior to 1940; and this conclusion would render inoperative the limitation of Section 122 (d)(5)."

In *Carter-Colton Cigar Co.* (1947) 9 T.C. 219, the Court correctly decided that the real property there involved was used in the trade or business of the taxpayer within the meaning of the statute when it was purchased by him for a business purpose despite the fact that:

> "* * * full or maximum use, of course, had not yet been made, and was finally prevented by latent developing circumstances over which Petitioner had no control.
>
> "Where the statute allows deductions for depreciation of property 'used in the trade or business' it has been held that 'used in the trade or business' means 'devoted to the trade or business' and includes all such property whether actually in use during the taxable year or not. *Kittridge* v. *Commissioner*, 88 F. 2d 632; *Yellow Cab Co. of Pittsburgh* v. *Driscoll*, 24 F. Supp. 993; *P. Dougherty Co.*, 5 T.C. 791-795. * * * its character as 'real property used in * * * trade or business continues after the planned use becomes impossible. *Solomon Wright, supra.*"

In *Solomon Wright, Jr.* (1947) 9 T.C. 173 the Tax Court concluded that real estate originally used for business did not become a capital asset merely because it had ceased to be property actively used in the taxpayer's business.

Despite the apparent views of the Tax Court to the contrary, the fact that petitioner as an individual

never held a real estate license is not significant to establish the property as a capital asset. *C. E. Mauldin* (1951) 16 T.C. 698, aff'd (CA 10, 1952) 195 F. 2d 714; *Gruver* v. *Commissioner* (CCA 4, 1944) 142 F. 2d 363; *Richards* v. *Commissioner* (CCA 9, 1936) 81 F. 2d 369; *King* v. *Commissioner* (CA 5, 1951) 189 F. 2d 122, cert. denied (1951) 342 U.S. 829.

Both the Tax Court and the Court of Appeals agree that petitioner acquired the property with the intention of developing it and selling lots. In this connection, they each recognize that he did everything humanly possible to succeed in his venture. Yet because at age 70, which he was in 1946, he was not demonstrating the same vigor he did nearly a quarter of a century earlier when he acquired the land they therefore seemingly conclude that as to him the property had become a capital asset.

And they nevertheless come to this conclusion despite making positive findings to the effect that his activity with respect to this property continued after its seizure in 1940 and through 1946, when his right of redemption was extinguished. For as the Tax Court stated: (App. 6a)

> "* * * moreover, his conduct in further attempting to sell the land after its seizure by Blair County and in offering to satisfy the mortgage outstanding against the property in May 1946, demonstrates his intention to retain control over it. * * *"

The findings and conclusions of the Tax Court, as well as those of the Court of Appeals are clearly erroneous. It is, therefore, the function of this Court to examine the foundation for these findings. *Baumgartner* v. *U.S.* (1944) 322 U.S. 665.

II. The Tax Court Improperly Disregarded the Uncontradicted Testimony of the Petitioner.

Where the testimony of an only witness is not contradicted, nor is he otherwise impeached and his testimony is not inherently improbable, it cannot be disregarded. On a petition to review a decision of the Tax Court where, as here, the facts were not in dispute but wrong legal conclusions were attached to them, the Court of Appeals is not bound to respect them but should draw different and correct conclusions of its own. *Wener* v. *Commissioner* (CA 9, 1957) 242 F. 2d 938.

The findings of fact made by the Tax Court in the instant proceeding conclusively establish that the property here involved was held primarily for sale to customers at all times until the equity of redemption was extinguished in 1946. As a matter of law it follows therefore that the property was an ordinary asset and the loss in 1946 can only be an ordinary loss. Upon the evidentiary facts found by the Tax Court, its ultimate conclusion as to the character of the property is clearly a *non sequitur*.

Where, neither the credibility of the witness nor conflicting facts are involved, a Court of Appeals is not bound by the legal conclusion of the Tax Court. In so far as the so-called ultimate fact is simply reached by processes of legal reasoning from, or the legal significance of, evidentiary facts, the required review is free from the restraining impact of the so-called "clearly erroneous rule," and it is the duty of the Appellate Court to draw its own inferences from undisputed facts. *Gamble* v. *Commissioner* (CA 5,

1957) 242 F. 2d 586; *Galena Oaks Corp.* v. *Scoffield,* CA 5 (1954) 218 F. 2d 217; and *McGah* v. *Commissioner,* CA 9 (1954) 210 F. 2d 769.

In *Foran* v. *Commissioner,* CA 5 (1948) 165 F. 2d 705, the Court of Appeals having determined that the conclusions of the Tax Court were based solely on the testimony of the taxpayer reversed and stated as follows:

> "The Tax Court believes everything that Foran said except his positive testimony * * * but it refused to accept his oath that the sale was thus caused and held it was for sale all the time in the course of his business. * * *
>
> "Here there is direct and positive evidence from the witness who best knows, that this property was for eighteen months being held as an investment and not held for sale to customers. His testimony is consistent with every proven fact. He gives a credible reason why it was not for sale and why finally in 1941 he did sell it. We think the court's refusal to follow the sworn testimony is contrary to law, and requires the setting aside of its fact-finding as it would that of a jury. We quote from Pennsylvania R.R. Co. v. Chamberlain, 288 U.S. 333, at page 340, 53 S. Ct. 391, 394, 77 L.Ed. 819, "And the desired inference is precluded for the further reason that respondent's right of recovery depends upon the existence of a particular fact which must be inferred from proven facts, and this is not permissible in the fact of the positive and otherwise uncontradicted testimony of unimpeached witnesses consistent with the facts actually proved, from which testimony it affirmatively appears that the fact sought to be inferred did not exist. This conclusion results from a consideration of many decisions, of which the following are examples: (citing cases).

A rebuttable inference of fact * * * 'must necessarily yield to credible evidence of the actual occurrence.'"

This Court in *Pennsylvania R.R. Co.* v. *Chamberlain* (1933) 288 U.S. 333 concluded that an inference of the existence of a particular fact from other proven facts is not permissible in the face of the positive and otherwise uncontradicted testimony of unimpeached witnesses consistent with the facts actually proved, from which testimony it affirmatively appears that the facts inferred did not exist.

The petitioner testified that he had been active in the real estate business for a period exceeding fifty (50) years and that this period of activity included not only the taxable year 1946 but also the forty (40) years preceding and approximately ten (10) years subsequent. The scope of this activity included not only the property here involved but simultaneously many other properties all of which taken together formed a continuous pattern going to make up his real estate business.

There is nothing of record to contradict the testimony of petitioner herein and the Tax Court therefore erred as a matter of law in disregarding the fundamental principle enunciated by this Court in *Pennsylvania R.R. Co., supra* and followed in *Foran* v. *Commissioner, supra.* In fact, the findings made by the Trial Court respecting the taxpayer's activities and their further conclusion that his continued activities after the property had been seized by public officials were so extensive as to negate an abandonment are clearly inconsistent with their ultimate finding that the

property was not held primarily for sale for the reason that he was inactive.

In any event, the Tax Court's finding in this respect is no more than *obiter dictum* for the reason that it ultimately concluded that no loss was allowable. In the circumstances, the conclusion that if a loss had been allowed it would have been a capital loss, not being necessary to their ultimate disposition in the case, it becomes a gratuitous conclusion and certainly not binding upon the appellate court.

CONCLUSION

The effect of the decisions below is to deny petitioner a business loss from a venture that he struggled with continuously through depressions and other adversities for more than twenty (20) years. His sole purpose in buying the property and trying thereafter to sell it was to make a business gain as the result of his risk and efforts. Instead of a gain, however, circumstances were such that an $11,000 loss was the result.

The facts found by the Tax Court and the Court of Appeals with respect to the purchase and persistent efforts thereafter to sell the Wopsononock property conclusively establish as a matter of law that this property was bought and held by Petitioner as a business asset and not as a capital asset. The conclusion to the contrary is an error that should be corrected by this Court.

Additionally, the Court of Appeals erred by not remanding these proceedings to the Tax Court for further testimony. See *Burns v. Commissioner, supra,*

> "* * * We are satisfied that under the theory applied in cases decided by the Tax Court to the

> effect that real estate acquired for use in a trade or business may not necessarily lose that status if plans to use it are frustrated, the Tax Court should, in this case consider this issue before it is passed on by this Court."

It is respectfully suggested that this Court should review these proceedings in order to resolve the hopeless conflict that presently exists as the result of the many irreconcilable Tax Court and Appellate Court decisions. The principle involved is of vital importance not only to petitioner but also to the many other taxpayers similarly situated. As stated by the former Chief Judge of the Tax Court in *Robert G. Elbert*, T. C. Memo. 1957-108.

> "The general question involved is one of the most litigated in the Tax Court."

A review of the instant record will establish that the facts as found by the Tax Court support his legal conclusion other than that petitioner was in the real estate business and the property involved was held by him primarily for sale to customers in the year 1946.

The Tax Court erred as a matter of law on the following grounds:

1. Their conclusion is not supported by, but is in fact contrary to and contradicted by their own evidentiary findings.

2. Their conclusion is contrary to the uncontradicted testimony of an otherwise unimpeached witness as to his intent with respect to the property.

The Court of Appeals erred as a matter of law on the following grounds:

1. They are not bound by a conclusion that is erroneous as a matter of law.

2. They are not bound by a finding of the lower court that was not necessary to its ultimate conclusion. The character of the loss as determined by the Tax Court was *obiter dictum* for the reason that they concluded that no less was allowable as a matter of law. Their voluntary expression as to the type of loss it might otherwise have been is not binding upon the appellate court.

Petitioner respectfully suggests that a remand would be desirable so as to enable the lower court to take further testimony in order that they might then make further and necessary findings after they have all of the material facts before them.

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Washington 5, D. C.
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WILTON H. WALLACE
Of Counsel

APPENDIX

27 T. C. No. 111

TAX COURT OF THE UNITED STATES

Docket No. 54804.

Filed March 11, 1957.

ROBERT H. MCNEILL, *Petitioner.*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

1. Deduction of loss realized by the owner of property upon seizure and sale for nonpayment of realty taxes to a corporation wholly owned by petitioner and his immediate family, *held*, precluded by section 24(b)(1)(B), I.R.C. 1939, as a sale between related taxpayers.

2. Debts incurred by a practicing attorney, which became worthless during 1947, *held*, not proximately related to his professional activities and deductible only as nonbusiness bad debts subject to the limitations of section 23(k)(4), I.R.C. 1939.

Wilton H. Wallace, Esq., and *Henry F. Lerch, Esq.*, for the petitioner.

Thomas N. Chambers, Esq., for the respondent.

WITHEY, *Judge:* The respondent determined deficiencies in petitioner's income tax for the indicated years as follows:

Year	Deficiency
1946	$2,762.66
1947	2,096.86

The issues presented for our decision are the correctness of the respondent's action (1) in disallowing a deduction claimed by petitioner as an abandonment loss in the amount of $11,000 arising from the sale of his land for nonpayment

of taxes and (2) in determining that bad debts in the amount of $2,685 are deductible only as nonbusiness bad debts. An additional issue presented by the pleadings concerning the deductibility of medical expenses is agreed by the parties to depend for its resolution solely upon our determination of the foregoing issues and accordingly is not further discussed.

ISSUE 1.

FINDINGS OF FACT.

Robert H. McNeill (sometimes hereinafter referred to as petitioner) is a resident of the District of Columbia and filed his income tax returns for 1946 and 1947 with the director of internal revenue at Baltimore, Maryland.

On November 29, 1924, petitioner acquired 834 acres of land located near Altoona, Pennsylvania, known as the Wopsononock properties, from Herman Van Senden and his wife. Petitioner previously had advanced funds to a contractor who was constructing a railroad across the land. In addition, petitioner guaranteed payment of a mortgage placed on the property by the contractor in favor of Van Senden. Upon default by the mortgagor, petitioner acquired the property at a foreclosure sale in order to protect himself from loss on the mortgage. At the time he acquired the property it was petitioner's intention to develop and subdivide the land and sell lots.

The purchase of the foregoing property was consummated by the execution by petitioner of two promissory notes in the amounts of $12,500 and $7,500 payable to H. W. Van Senden and Harry Lamson, respectively, the execution of a mortgage as security for payment of the notes and a bond in the amount of $40,000. Petitioner eventually paid $14,500 on the two notes.

He desired to sell the lots to the public either at auction or through separate sales transactions. Petitioner engaged

experienced engineers to survey the property and prepare plats of the land to be offered for sale.

At a cost of $3,000, McNeill built a road through the forest to the top of the plateau where the lots held for sale were located.

Petitioner repeatedly advertised for the sale of the lots. He employed a prominent realtor in the community to solicit sales of the property, and made extensive efforts over a period of several years to sell the lots. All such efforts were completely unsuccessful.

Attempts were made to construct an airport project within the area, and also to interest the State of Pennsylvania in developing a public park on the land, but without success. Petitioner's expenses in connection with his attempt to develop an airport on the land amounted to $2,500.

In 1940 the Commissioners of Blair County, Pennsylvania, seized 458 acres of the property in question because of nonpayment of realty taxes and retained title thereto for 2½ years, attempting meanwhile to sell it to a private owner after failing to dispose of the property to a public bidder for an amount equal to the unpaid taxes. During 1942 the property was conveyed by the County Commissioners to the City of Altoona, Pennsylvania. After the acquisition of 458 acres of the Wopsononock tract by Blair County, and later by the City of Altoona, petitioner continued his efforts to sell all or part of the land, since he retained a right of redemption therein.

In May 1946, petitioner made an offer to the Estate of H. W. Van Senden to satisfy the mortgage outstanding against the Wopsononock property in the amount of $5,000 by payment of that amount, but the offer was rejected. The City of Altoona, eventually offered to sell the property to petitioner. Through petitioner's intervention, on December 5, 1946, title to the property was transferred from the City of Altoona directly to the Royal Village Corporation

in consideration of $750, an amount less than the unpaid real estate taxes outstanding against the property.

At the time of the sale of the property in question to the Royal Village Corporation, petitioner's right of redemption in the property expired and he thereby lost his opportunity to recover his investment therein.

The capital stock of the Royal Village Corporation as of December 5, 1946, was held as follows:

Name	Relationship	Shares
Robert H. McNeill		150
Cora B. McNeill	Wife	141
Frances A. Easley	Daughter	5
George H. McNeill	Son	5
		301

During 1952 petitioner paid $5,250 to the Estate of H. W. Van Senden in full settlement of all claims of that estate against him with respect to the Wopsononock property and in full satisfaction of the outstanding mortgage thereon. The title to the Wopsononock tract remained in the Royal Village Corporation from the time of its acquisition on December 5, 1946, and was held by the corporation at the time of the foregoing payment by petitioner.

While practicing law in Washington, D. C., petitioner has participated in a number of real estate developments in Maryland, Virginia, the District of Columbia and North Carolina. In addition, he occasionally has promoted and financed the construction of various buildings, including office buildings in Washington, D. C. However, petitioner has never held a real estate license.

In his individual income tax return for 1946, petitioner deducted $11,000 as a loss arising from the abandonment of the Wopsononock property because of the expiration of his right of redemption therein during that year.

Petitioner has not in fact abandoned the Wopsononock property. Further, petitioner was not engaged in the real estate business during the years in issue and the tract of land here involved was not held by him primarily for sale to customers in the ordinary course of his trade or business at the time of its sale by the City of Altoona on December 5, 1946.

OPINION

Respondent disallowed the deduction in the amount of $11,000 taken by petitioner on his income tax return for 1946 on the grounds, first, that petitioner had not in fact abandoned the property in question and, second, that the transaction constituted an indirect sale between related taxpayers and recognition of the loss is therefore prohibited by section 24 (b)(1)(B) of the Internal Revenue Code of 1939.[1]

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[1] SEC. 24. ITEMS NOT DEDUCTIBLE.

* * * * * *

(b) Losses From Sales or Exchanges of Property.—

(1) Losses disallowed.—In computing net income no deduction shall in any case be allowed in respect of losses from sales or exchanges of property, directly or indirectly—

* * * * * *

(B) Except in the case of distributions in liquidation, between an individual and a corporation more than 50 per centum in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual;

* * * * * *

(2) Stock ownership, family and partnership rule.—For the purposes of determining in applying paragraph (1), the ownership of stock—

* * * * * *

(B) An individual shall be considered as owning the stock owned, directly or indirectly, by or for his family;

* * * * * *

(D) The family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants; * * *

In the alternative, respondent asserts that if any loss is allowable it is at most a long-term capital loss arising from the sale during 1946 of a capital asset, relying upon the decision of the Supreme Court in *Helvering* v. *Nebraska Bridge Supply & Lumber Company*, 312 U.S. 666.

Petitioner contends that upon the expiration of his right of redemption in the property during 1946 and the sale thereof to the Royal Village Corporation, he sustained a business loss, deductible in full for that year.

In his petition and opening statement, petitioner took the position that the loss arose from his abandonment of the Wopsononock property. On brief, his principal argument is that at the time of sale to the Royal Village Corporation in 1946, the property in question was held by him primarily for sale to customers in the ordinary course of his trade or business, and that the resulting loss was an ordinary loss rather than a capital loss.

In order to establish the abandonment by petitioner of his property, it is incumbent upon him by reference to the surrounding circumstances to show the occurrence of an act or event disclosing his intention to abandon. *Talache Mines, Inc.* v. *United States*, 218 F. 2d 491; *Belridge Oil Co.*, 11 B.T.A. 127; *Reuben H. Donnelley Corporation*, 26 B.T.A. 107; *W. B. Davis & Son, Inc.*, 5 T.C. 1195. Mere discontinuance of use alone is insufficient. *W. B. Davis & Son, Inc., supra.* The record herein discloses no evidence of voluntary abandonment by petitioner of his land. He simply acquiesced in the action of Blair County, Pennsylvania, in seizing the property in 1940. Moreover, his conduct in further attempting to sell the land after its seizure by Blair County and in offering to satisfy the mortgage outstanding against the property in May 1946 demonstrates his intention to retain control over it. Such conduct is clearly inconsistent with abandonment.

We are likewise unable to agree with petitioner's contention that the property at the time of its sale by the

City of Altoona, Pennsylvania, was held by him primarily for sale to customers in the ordinary course of his business. Petitioner has never held a real estate license. The record herein does not clearly disclose the frequency, continuity, and substantiality of his sales of real estate or the extent of his real estate activities generally. So far as herein appears, petitioner has never held himself out to the public as being engaged in any phase of the real estate business. *Cf. Home Co., Inc.* v. *Commissioner*, 212 F. 2d 637; *Dunlap* v. *Oldham Lumber Co.*, 178 F. 2d 781; *W. T. Thrift, Sr.*, 15 T.C. 366; *Arthur E. Wood*, 25 T.C. 468. Moreover, he had not sold so much as one parcel of the Wopsononock tract since the time of its acquisition in 1924. We are therefore unable to find that the land in question at the time of sale was held by petitioner for sale to customers in the ordinary course of his trade or business.

In *Helvering* v. *Nebraska Bridge Supply & Lumber Co.*, *supra*, the Supreme Court reversed a decision of the United States Court of Appeals for the Eighth Circuit and held that a loss arising from the expiration of the taxpayer's equity of redemption in lands foreclosed by the state for delinquent realty taxes was a loss arising from a sale within the meaning of section 117 of the Revenue Act of 1934, a provision similar in effect to section 117 of the 1939 Code. Accordingly, any loss resulting from the expiration of his equity of redemption in the land in question by petitioner herein is in the nature of a capital loss and, if allowed, is subject to the limitations of section 117(d) of the 1939 Code.

With respect to the respondent's contention that section 24(b)(1)(B) of the Code precludes the allowance of any deduction for the loss in question, the terms of that section provide that—

> no deduction shall in any case be allowed in respect of losses from sales or exchanges of property, directly or indirectly * * * between an individual and a corporation more than 50 per centum in value of the

outstanding stock of which is owned, directly or indirectly, by or for such individual * * *.

The petitioner acquired the Wopsononock property by deed on November 29, 1924. The authorities of Blair County, Pennsylvania, seized the property because of delinquent taxes on January 30, 1940, and conveyed it to the City of Altoona in 1942, which in turn sold it to the Royal Village Corporation on December 5, 1946. Petitioner's right of redemption in the property was terminated as of the latter date. 72 Pa. Stat. § 6105.1. Petitioner holds one share less than 50 per cent of the Royal Village stock, and his wife, son and daughter hold the balance. It is clear that petitioner and the corporation are related taxpayers within the meaning of section 24(b)(1)(B), and the sale issue remaining is the question whether the aforementioned transaction constitutes a sale or exchange between them, directly or indirectly.

In support of his position, the petitioner relies on the decision of the United States Court of Appeals for the Seventh Circuit in *McCarty* v. *Cripe*, 201 F. 2d 679. The taxpayer there was engaged in the business of buying and selling real estate. He purchased in 1916 a tract of undeveloped farm land with the intention of subdividing it and selling lots. In 1943 proceedings for the foreclosure of liens on the property for delinquent improvement assessments and realty taxes were commenced by Cuyahoga County, Ohio, where the land was located. Subsequently, the land was sold at public auction. Approximately 25 bids were received and the property was awarded to the highest bidder who paid for it with funds furnished by the taxpayer. The purchaser subsequently conveyed the land to a corporation which was controlled by the taxpayer, who owned more than 50 per cent of the outstanding stock thereof. The land was situated adjacent to another tract which the corporation owned and was developing for residential purposes.

The taxpayer there, as here, took the position that his investment in the property so conveyed was deductible as a business loss, as a consequence of the foregoing transaction. The Court of Appeals upheld his contention on the grounds, first, that the foreclosure sale was involuntary and the taxpayer therefore could not have selected the time for the realization of a loss, second, that there was no evidence of prearrangement between the decedent and his corporation and, finally, that the land was sold at a public auction at which the bidding was spirited and there was consequently a strong presumption that the property sold for not less than its fair market value.

In the instant case, however, the property was not sold at a public auction. We have found as a fact that title to the property was conveyed directly to the Royal Village Corporation because of petitioner's intervention. Thus, his loss resulted from his action in causing the tract of land in question to be conveyed to that corporation. Had he accepted a conveyance himself he would have realized no loss.

In addition, it is difficult for us to find here that there is no evidence of prearrangement between the petitioner and his corporation, as was held by the Court of Appeals in *McCarty* v. *Cripe, supra.*

Since petitioner here was without competition in bidding for the property, we cannot presume that the price paid for the land was equal to its fair market value.

Finally, as previously noted, we are unable to find that petitioner herein was engaged in the business of buying and selling real estate at the time of the sale in question, as was the case in *McCarty* v. *Cripe, supra.*

For the foregoing reasons, we are of the opinion that *McCarty* v. *Cripe, supra,* is not controlling of the situation here presented.

In *McWilliams* v. *Commissioner,* 331 U.S. 694, the taxpayers, husband and wife, each sold stock on the open

market and shortly thereafter each purchased like shares in the same company. At the time the orders for sale were placed by each taxpayer for his individual account, the broker was instructed to purchase a like number of the same shares at as near the same price as possible for the account of the other. The stock certificates subsequently acquired at the time of purchase were different from those previously sold. In each instance the broker was advised that the sale was for the purpose of establishing a tax loss. Each taxpayer deducted the losses resulting from the foregoing sales in his individual income tax return. In holding that such losses were not deductible because the sales were indirect sales between husband and wife, the Supreme Court described the congressional policy and purpose underlying the enactment of section 24(b) of the 1939 Code as follows:

> Section 24(b) states an absolute prohibition—not a presumption—against the allowance of losses on any sales between the members of certain designated groups. The one common characteristic of these groups is that their members, although distinct legal entities, generally have a near-identity of economic interests. It is a fair inference that even legally genuine intra-group transfers were not though to result, usually, in economically genuine realizations of loss, and accordingly that Congress did not deem them to be appropriate occasions for the allowance of deductions.
>
> * * * * * * *
>
> We conclude that the purpose of § 24(b) was to put an end to the right of taxpayers to choose, by intra-family transfers and other designated devices, their own time for realizing tax losses on investments which, for most practical purposes, are continued uninterrupted.

We are unable to conclude from the record before us that the sale in question created an actual break in the continuity of petitioner's investment. That petitioner regarded his investment in the land as surviving the sale to the

Royal Village Corporation is indicated by the fact that he personally satisfied the outstanding mortgage in 1952, rather than the corporation. Further, as we have previously mentioned, petitioner was offered the property by the City of Altoona and had he accepted a deed in his own name, he would not have realized a loss. Without his influence and intervention the conveyance to the Royal Village Corporation would not have been made. We are not convinced from the record herein that petitioner here, as in *McWilliams* v. *Commissioner, supra,* did not actually negotiate the sale for the purpose of creating a tax loss. *Cf. DuPont* v. *Commissioner,* 118 F. 2d 544; *Bank of America National Trust & Savings Association,* 15 T.C. 544, affd. 193 F. 2d 178; *Crown Cork International Corporation,* 4 T.C. 19, affd. 149 F. 2d 968. Moreover, the record does not show that petitioner would not have been able to postpone the sale to the Royal Village Corporation on December 5, 1946, until a subsequent year and thereby select the time for the realization of his loss. Accordingly, the transaction here in issue appears to fall within the scope of the congressional policy expressed in section 24(b) of the 1939 Code, and, in our view, was a type which Congress by the enactment of that section intended to reach.

A question similar to the issue herein was presented for our decision in *Thomas Zacek,* 8 T.C. 1056. The taxpayer there owned a fractional interest in mortgaged property upon which the mortgage interest and realty taxes became delinquent. The mortgagees, who were brothers of the taxpayer, commenced foreclosure proceedings in the Nebraska courts, which the mortgagors resisted. The court ordered a foreclosure sale of the property and it was sold to the mortgagees for an amount equal to the outstanding mortgage principal and interest, taxes and costs. The taxpayer claimed a deduction for his share of the loss from the foreclosure sale of the property as a long-term capital loss. The respondent disallowed the loss on the ground that the foreclosure sale constituted a sale

between members of a family, within the meaning of section 24(b)(1)(A) of the 1939 Code. We there held that the language of section 24(b)(1)(A) included involuntary sales and that the transaction in question constituted a sale of property indirectly between members of a family, thus precluding the deduction of any loss arising therefrom.

We are of the opinion that our holding in *Thomas Zacek, supra*, is dispositive of the issue here presented. Prior to the sale of the Wopsononock property to the Royal Village Corporation in 1946, petitioner retained a right of redemption therein. When petitioner was offered the property by the trustee of the City of Altoona, Pennsylvania, for $750, instead of accepting title in his own name he caused title to be transferred to a corporation wholly owned by himself, his wife and immediate family. Although he did not himself actually sell the property to the Royal Village Corporation, through his direct intervention alone title was conveyed to the corporation. Consequently, we are of the opinion that section 24(b)(1)(B) of the Code is applicable to the sale in issue and the allowance of a capital loss realized thereon is by that section prohibited.

ISSUE 2

Findings of Fact

Petitioner's business was that of a practicing attorney. He was not in the business of lending money.

Petitioner made 2 loans to Leslie D. Measell during 1947, the first on May 22, and the second on July 18, in the amounts of $1,450 and $650, respectively. The $1,450 loan subsequently was reduced by payments of the creditor to $525. In addition he endorsed a check in the amount of $100 drawn by Leslie D. Measell on February 20, 1947, and subsequently was required to satisfy the payee.

Measell was a real estate agent who had sold real estate for petitioner. He was also a client of petitioner. Measell

was frequently in straitened financial circumstances, particularly during 1947. It was his practice as a real estate agent to endeavor to collect his commissions in advance or to attempt to assign his rights to commissions at a discounted figure. On a number of occasions he contacted petitioner concerning the assignment of commissions at a discount prior to their receipt and petitioner purchased several such assignments. All of the assignments purchased by petitioner during 1947 proved to be fictitious. Petitioner attempted to collect the loans made to Measell during 1947, and brought suit against him, but was unable to collect on the judgment. Petitioner charged off $1,275, representing the unpaid balances on the 3 foregoing obligations, during 1947 and deducted that amount on his income tax return for that year as a business bad debt.

Petitioner also loaned $400 to Arthur L. Langston, Jr., on June 7, 1947, in exchange for a 90-day promissory note. Langston was a son-in-law of Measell and was employed by him in his real estate business. Langston paid $50 on the foregoing note leaving an unpaid balance of $350. Petitioner was unsuccessful in his attempts to collect the unpaid balance of the loan during 1947 and charged off the debt during that year. Petitioner deducted the unpaid balance of the loan as a business bad debt on his return for 1947.

Petitioner charged off $360 during 1947 arising from his liability as endorser of a promissory note drawn by Charles E. Marsh. Marsh was a client of petitioner and Secretary to the Columbia Title Company. Petitioner valued his relationship with Marsh because of his affiliation with the Columbia Title Company. Marsh died shortly after the endorsement of the foregoing note and petitioner was required to satisfy the face amount of the note, with interest. He deducted $360 thus paid by him as endorser as a business bad debt on his income tax return for 1947.

During 1947 petitioner charged off $250 representing the balance of a promissory note drawn in petitioner's favor

by Tom Kinnevey on March 25, 1946. Kinnevey was an assistant to an attorney who rented office space to petitioner. A deduction in the amount of $250 was claimed by petitioner as a business had debt on his 1947 return.

Petitioner further charged off $450, representing the unpaid balance on a promissory note drawn by Kelly Kash, which petitioner endorsed. Kash was an attorney who shared office space with petitioner. Petitioner normally referred to Kash the overflow of his business, but Kash was unable to make a living practicing law and petitioner endorsed the foregoing note in order to assist him in alleviating his financial difficulties. Kash subsequently died while residing in the State of Kentucky and petitioner was unable to collect the unpaid balance of the note. Accordingly, he deducted $450 as a business bad debt on his return for 1947.

OPINION

Petitioner claimed a total deduction of $2,685 in his income tax return for 1947 representing bad debts arising from individual loans and accommodations endorsements of checks and promissory notes. Petitioner contends that the loans were incurred in connection with his business as a practicing attorney and that they therefore constitute business debts which became worthless during 1947. Respondent does not question the worthlessness of the debts or the year in which they are deducted as worthless, but contends that they represent nonbusiness bad debts and are consequently subject to the limitations of section 23 (k)(4) of the 1939 Code.

The purposes of petitioner's advances and endorsements and his relationship with the debtors were meagerly described at the hearing. We are unable to conclude from the record that the aforementioned loans bore a proximate relationship to petitioner's law practice, either at the time the loans were made or at the time they became

worthless. We are convinced also that he was not in the business of lending money and that the transactions here involved are isolated in character. Since petitioner has failed to establish that the foregoing transactions were related to his professional activities as an attorney, we must agree with respondent's contention that the debts in question were personal in nature and are deductible only as nonbusiness bad debts under section 23(k)(4) of the 1939 Code. *Putnam* v. *Commissioner*, 224 F. 2d 947, affd. 352 U.S. 82. *Cf. Stuart Bart*, 21 T.C. 880.

Decision will be entered for the respondent.

* * * * * * * * * *

Decision.

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, filed March 11, 1957, it is

ORDERED AND DECIDED: That there are deficiencies in income tax for 1946 and 1947 in the amounts of $2,762.66 and $2,096.86, respectively.

Entered: March 12, 1957

(Signed) G. G. WITHEY
Judge

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 7527.

ROBERT H. MCNEILL, *Petitioner*,

versus

COMMISSIONER OF INTERNAL REVENUE, *Respondent*

On Petition to Review the Decision of The Tax Court of the United States.

(Argued November 22, 1957. Decided January 11, 1958.)

Before SOPER and HAYNSWORTH, Circuit Judges, and R. DORSEY WATKINS, District Judge.

Wilton H. Wallace (Henry F. Lerch and Wallace & Lerch on brief) for Petitioner, and Charles B. E. Freeman, Attorney, Department of Justice, (Charles K. Rice, Assistant Attorney General, Lee A. Jackson and A. F. Prescott, Attorneys, Department of Justice, on brief) for Respondent.

SOPER, Circuit Judge:

Robert H. McNeill, the taxpayer in this case, is a lawyer who for many years has practiced his profession in Washington, D. C. He has also been interested in real estate, and in the pursuit of this line of activity he acquired a large tract of land near Altoona, Pennsylvania, which he

intended to subdivide and to sell in lots. The venture proved unsuccessful despite repeated efforts on his part and the land was finally seized and sold at a loss for taxes. The present controversy raises the question whether the taxpayer is entitled under the federal statutes to deduct the loss from his taxable income for the year 1946.

A minor question is whether the taxpayer is entitled to a deduction from income in 1947 for losses in that year from bad debts due him for certain loans to individuals and certain accommodation endorsements for their benefit.

The Pennsylvania project involved 834 acres of land, a portion of which had already been divided into lots and sold. The taxpayer acquired the property at a mortgage foreclosure sale in 1924. He gave in payment his promissory notes for $12,500 and $7,500 secured by mortgage on the land. He had lost money through advances to the prior owner and hoped to recoup his loss by further subdividing and selling the land. For this purpose the land was surveyed, plats showing the division into lots were prepared, and a road was built leading to the plateau on which the land was located to make the property more accessible. The taxpayer also employed a prominent realtor in the community to solicit sales of the lots, and extensive efforts were made by advertisement and otherwise to sell the lots over a period of several years. In 1925, elaborate plans for an auction sale were made and it was well attended, but nothing was accomplished since the crowd was suddenly dispersed by a violent storm. Subsequent attempts were made to establish a public park and also to develop an airport project in the area, and efforts to interest the governmental authorities were made, but these projects also fell through. No lots were ever sold by the taxpayer, and the project lay dormant for a number of years.

Eventually, in 1940, the commissioners of Blair County, Pennsylvania, seized the property because of nonpayment of taxes and held title to it for a period of two and one-half

years, during which they attempted, without success, to sell it for an amount equal to the unpaid taxes. Under Pennsylvania law the taxpayer had the right to redeem the land by payment of the taxes within certain periods (Purdon's Pennsylvania Statutes, §§ 5971(p), 5971(q) and 6105.1) and he made certain efforts to sell all or part of the land but was unsuccessful. The tax authorities had no better success in their efforts to sell after the expiration of the redemption period and finally, in 1946, more than six years after the seizure, they offered to sell the property to the taxpayer for $750.00, and for this sum the property was transferred, through the intervention of the taxpayer, directly to the Royal Village Corporation, in which all of the stock was held by the taxpayer and members of his family. The transfer was made by deed on December 5, 1946, and the taxpayer accepted this as the date of the realization of his loss and deducted it in his 1946 income tax return. Six years later, in 1952, the taxpayer *paid* $5,250 to the estate of the mortgagee of the property in full satisfaction of the outstanding mortgage thereon at that time. The Royal Village Corporation then held title to the property.

The Commissioner disallowed the loss on the ground that the final transaction constituted an indirect sale by the taxpayer to a corporation in which more than 50 per cent in value of the outstanding stock was owned by members of his family, and hence the loss was not deductible under § 24(b) (1)(B) of the Internal Revenue Code, 1939. The Tax Court affirmed this holding. Undoubtedly it was correct if the loss was realized by a sale of the property by the taxpayer to the family corporation. The statute was designed to put an end to the right of taxpayers to choose their own time for realizing tax losses on investments by intra-family transfers and other designated devices. *McWilliams* v. *Commissioner*, 331 U.S. 694; *Commissioner* v. *Kohn*, 4 Cir., 158 F. 2d 32. The fact is, however, that the loss was not occasioned by the transfer of the property to the Royal Village Corporation. It was brought

about by the seizure and sale of the property for taxes after unsuccessful efforts by the county authorities during a six-year period. Of course the true nature of the transfer rather than the form which is took is controlling, but there is nothing in the evidence to warrant the inference that McNeill controlled the Pennsylvania authorities so that in effect the seizure and sale for taxes were his actions and not theirs, or that their subsequent attempts to sell the land were not genuine efforts to satisfy the tax lien, or that their final offer to sell the property to the taxpayer was made in collusion with him to serve his purposes. The failure of the project as a real estate development is proved by the uncontradicted evidence which covers a period of sixteen years prior to the seizure for taxes and six years thereafter, at the end of which the property was offered and sold to the taxpayer. It is quite impossible to find in this evidence the sort of conduct which characterizes family transfers made for the purpose of realizing tax losses and at the same time retaining the investments. The realization of the loss in this instance was not brought about by an arrangement between the taxpayer and the corporation which he controlled but was due to the separate and independent action of the public authorities in the collection of overdue taxes. A similar conclusion was reached under like circumstances in *McCarty* v. *Cripe*, 7 Cir., 201 F. 2d 679; cf. *Zacek* v. *Comm'r*, 8 T.C. 1056.

There is the further question whether the loss was deductible as one incurred in the operation of the real estate business by the taxpayer or should be considered a capital loss on his investment and therefore subject to the limitations imposed upon losses of this character. The Tax Court made the finding that the taxpayer was not engaged in the real estate business during the years in issue and that the Altoona land was not held by him primarily for sale to buyers in the ordinary course of his business at the time of the tax sale in 1946. We are bound by this

finding since it was not clearly erroneous. During the years immediately following the acquisition of the Pennsylvania property in 1924, the taxpayer made diligent efforts to sell the land in lots and may fairly be considered to have been engaged in the real estate business at that time; but after this period the operation ceased. The subsequent attempts to dispose of the land for a public park or an airport also came to an unsuccessful end in the late '20s or early '30s. The testimony of the taxpayer as to what he did thereafter is confined to the general statement that he tried to dispose of the property and is entirely consistent with the conclusion of the Tax Court that the project was a failure and the Taxpayer did not operate it as a business in 1946, when the loss was claimed. The taxpayer supplements his testimony on this point by referring to numerous activities by him in the real estate field in various localities in or adjacent to Washington and in neighboring states, but most of these transactions took place prior to 1930 and all of them occurred many years before the tax year in question. In our judgment the tax deduction should be allowed only as a caiptal loss.

The taxpayer also made deductions in his tax return for 1947 of certain bad debts on the theory that they were business bad debts deductible under § 23(k)(1) of the Internal Revenue Code, 1939. The Commissioner disallowed the deductions as business bad debts but allowed them as non-business bad debts under § 23(k)(4) and the Tax Court sustained the Commissioner. Seven loans in the aggregate sum of $2,685 were made to five persons, three of whom were clients in or associated with the real estate business and two were office associates of the taxpayer in the practice of law. The taxpayer testified that he regarded these loans as helpful to him in his business as a practicing lawyer. The relationship of the loans, however, to the taxpayer's practice is not clearly shown and it may fairly be inferred that the moneys were advanced to aid friends of the taxpayer who for the time being were in distress. We do not think that it can be said that the

Tax Court was clearly wrong in reaching the conclusion that the transactions were not related to the professional activties of the taxpayer as an attorney but were personal in nature and therefore deductible only as nonbusiness bad debts.

The decision of the Tax Court is reversed and the case remanded for further proceedings consistent with this opinion.

Reversed.

Judgment

Filed and Entered January 11, 1958

UNITED STATES COURT OF APPEALS, FOR THE FOURTH CIRCUIT

No. 7527

ROBERT H. MCNEILL, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

ON PETITION to Review the Decision of The Tax Court of the United States.

THIS CAUSE came on to be heard on the record from The Tax Court of the United States, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the decision of the said The Tax Court of the United States, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to The Tax Court of the United States for further proceedings consistent with the opinion of the Court filed herein.

January 11, 1958.

MORRIS A. SOPER
United States Circuit Judge

February 5, 1958, petition of petitioner for extension of time to file petition for rehearing filed.

Order Extending Time to File Petition for Rehearing and Staying Mandate

Filed February 7, 1958

(Style of Court and Title Omitted.)

Upon the application of the petitioner, and for good cause shown,

It is ordered that the time within which the petitioner may file a petition for a rehearing in the above entitled case, be, and it is hereby, extended to and including March 1, 1958.

It is further ordered that the mandate be, and it is hereby, stayed pending the timely filing of the petition for a rehearing.

February 6th, 1958.

JOHN J. PARKER
Chief Judge, Fourth Circuit.

Filed Mar. 1, 1958

IN THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

No. 7527

ROBERT H. MCNEILL, *Petitioner*,

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

Petition for Rehearing, or in the Alternative for a Modification of the Mandate to Order the Court Below to Take Further Testimony

TO THE HONORABLE, UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT:

This Petition for a rehearing of the appeal herein, or in the alternative for a modification of the mandate so as to order the Court below to take further evidence, is based on the following grounds:

I. This Court Is Not Bound by the Tax Court's Clearly Erroneous Finding of Fact That the Petitioner Was Not Engaged in the Real Estate Business During the Taxable Years 1946 and 1947

A. Background

On his income tax return for the taxable year 1946 the petitioner deducted $11,000.00 as an ordinary loss resulting from real estate in Pennsylvania.

Respondent's position prior to the trial in 1956 was limited to questioning the cost basis of the property;

whether or not the property had been abandoned, and if so, in what year; and whether, in any event, the loss should not be disallowed in full as resulting from a transaction between related taxpayers.

The explanation given in the statutory notice of deficiency for the disallowance of the deduction was merely as follows:

> "The claimed deduction of $11,000 alleged to represent a loss incurred in connection with certain real estate is disallowed as not representing an allowable deduction for federal tax purposes."

Petitioner's preparation for the Tax Court trial, which lasted only two hours, was limited to answering respondent's previously stated objections to the deduction. He was surprised therefore when for the first time the respondent, on opening statement, raised the still further alternative defense, that the loss, if any, should be limited as a capital loss.

B. Record Before the Tax Court

The only witness to testify before the Tax Court was the taxpayer and his uncontradicted testimony is to the effect that:

(1) He has been active in the real estate business continuously for approximately 50 years.

(2) This period of activity included not only the taxable years involved (1946 and 1947) but also each of the approximately 40 years preceding and 10 years subsequent thereto.

(3) The scope of this activity included not only the property in Pennsylvania but simultaneously many other properties, all of which together formed a continuous pattern going to make up his "real estate business."

The Tax Court summarily denied petitioner's Motion for Reconsideration filed promptly after the opinion of that Court was handed down.

C. Petitioner's Allegation of Errors

It is petitioner's view that the Tax Court incorrectly held that the facts of record, all of which were undisputed, support the finding that he was not in the Real Estate business during 1946. To so conclude, the Tax Court not only disregarded the petitioner's uncontradicted testimony respecting the Pennsylvania property in this year,[1] but also disregarded the related history of his other activities in this and prior years.[2]

1. The Tax Court improperly disregarded the uncontradicted testimony of the petitioner

Where the testimony of an only witness is not contradicted and he is not otherwise impeached, and his testimony is not inherently improbable, it cannot be disregarded even though he is an interested party. On petition to review the decision of the Tax Court when, as here, the facts are not in dispute but wrong legal conclusions are attached to them, the Court of Appeals is not bound to

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[1] "Q. You testified regarding your attempts to sell those lots over the years. Did you continue to try to sell these lots up to the time the property was deeded by the tax authorities to Royal Village Corporation? A. Indeed, I did." (Appendix 18a.)

[2] "And sometimes I go wrong, sometimes right, but I have been in that business [real estate] continuously since I came to Washington". (1903.) Appendix 9a.

"* * * As to buildings, I could mention several others, Your Honor, but in North Carolina I developed two or three properties, and I own a property now in Virginia for development purposes." Appendix 9a.

"* * * I don't think there has been a year I haven't been active in real estate around Washington". Appendix 10a.

respect them, but should draw different and correct conclusions of its own. *Wener* v. *C. I. R.*, (C. A. 9th, 1957) 242 Fed. 2d. 938. The findings of fact by the Tax Court show that Petitioner was offering the Altoona land for sale at all times until his title was lost.

The question as to whether property was held by the taxpayer primarily for sale, in the ordinary course of business, is principally a fact question and one where the Tax Court has the function of making the original determination through the process of weighing and balancing conflicting facts and factors, and drawing from these the inferences and conclusions upon which to base its decision.

Where, however, neither the credibility of the witness, nor conflicting facts are involved, this Court is in as good a position as the Tax Court, insofar as the so-called ultimate fact is simply reached by processes of legal reasoning from, or the legal significance of the evidentiary facts, it is required to review free from the restraining impact of the so-called "clearly erroneous rule". *Gamble* v. *C. I. R.*, (C. A. 5th—1957) 242 Fed. 2nd. 586; *Galena Oaks Corp.* v. *Scofield*, (C. A. 5th—1954) 218 Fed. 2d. 217. It is clear that the Court of Appeals should draw its own inferences from undisputed facts. *McGah* v. *C. I. R.* (C. A. 9th —1954) 210 Fed. 2d. 769.

In *Foran* v. *C. I. R.* (C. C. A. 5th—1948) 165 Fed. 2d. 705, in finding that the conclusions of the Tax Court were based on only the testimony of the taxpayer, the Court in reversing relied on the Supreme Court's decision in *Pa. R. R. Co.* v. *Chamberlain, etc.*, and stated as follows:

> "The Tax Court believed everything that Foran said except his positive testimony * * * but it refused to accept his oath that the sale was thus caused, and held it was for sale all the time in the course of his business.
>
> "* * * Here there is direct and positive evidence from the witness who best knows, that this property

was for eighteen months being held as an investment and not held for sale to customers. His testimony is consistent with every proven fact. He gives a credible reason why it was not for sale and why finally in 1941 he did sell it. We think the court's refusal to follow the sworn testimony is contrary to law, and requires the setting aside of its fact-finding as it would that of a jury. We quote from Pennsylvania R. R. Co. v. Chamberlain, 288 U. S. 333, at page 340, 53 S. Ct. 391, 394, 77 L. Ed., 819, 'And the desired inference is precluded for the further reason that respondent's right of recovery depends upon the existence of a particular fact which must be inferred from proven facts, and this is not permissible in the face of the positive and otherwise uncontradicted testimony of unimpeached witnesses consistent with the facts actually proved, from which testimony it affirmatively appears that the fact sought to be inferred did not exist.' This conclusion results from a consideration of many decisions, of which the following are examples: [citing cases]. A rebuttable inference of fact * * * 'must necessarily yield to credible evidence of the actual occurrence.' We recognize that intent may be proved by circumstances, and that a party's testimony as to his intent may be rebutted by proof of circumstances which are inconsistent therewith. We held that no circumstance found by the Tax Court here is inconsistent with the reasonable and uncontradicted testimony of Foran."

2. The Tax Court's ultimate finding of fact is clearly erroneous as a matter of law

Mere discontinuance of the active use of real estate does not change its character previously established as business property. *Alfred Kruse* (1957) 29 T. C. No. 51.

The rationale of the Tax Court in *Alfred Kruse, supra,* follows *Walter G. Morley* (1947) 8 T. C. 904, 915, wherein on facts not unlike those here involved the Tax Court stated as follows:

> "None of these transactions was 'an isolated holding dissimilar from any other transaction and unrelated to the history of petitioner's activities.'"

"* * * Petitioner's activity was not restricted or halted by reason of any change in his plans or purpose, but rather by the force of economic circumstances beyond his control and not of his making. The general business depression of the past decade was the reason for the curtailment of petitioner's activity. We cannot ignore the realities of the situation. (p. 916)"

"* * * While we incline to the view that the business of selling real estate was one regularly carried on by petitioner in 1940 (the year involved), it is not necessary to our conclusion on this point for us to hold, or find, that the losses in question were attributable to the operation of a business regularly carried on by the taxpayer *in that year*. It is sufficient for our conclusion that we find, as we have done, that the losses in question were attributable to the operation of a business regularly carried on by petitioner (citing cases. There can be no question but the business of buying and selling real estate was regularly carried on by petitioner prior to 1931. The properties here in question were purchased or acquired by petitioner for re-sale at a profit before that date. Even though we should assume *arguendo* that the business of selling real estate, although engaged in by petitioner in 1940, was not one regularly carried on by him in that year, nevertheless, we would conclude that the losses in question were attributable to a business of buying and selling real estate which was regularly carried on by him in years prior to 1940; and this conclusion would render inoperative the limitation of Section 122 (d) (5)." 8 TC 917

The Tax Court has here taken the narrow position that the particular property in Pennsylvania was not used by taxpayer in his trade or business and in so concluding ignores not only the realities of the economic adversity that affected this property, but also treats the taxpayer's activities with respect to this property as having no relationship to his other properties and real estate activities. No proper determination as to the existence of a "trade or business" can be made by merely considering some of the

pertinent facts while at the same time disregarding related facts and similar business activities.

In *Carter-Colton Cigar Co.* (1947) 9 T. C. 221, the Court correctly decided that the real property there involved was used in the trade or business of the taxpayer within the meaning of the statute when it was purchased by him for a business purpose, despite the fact that,

> "Full or maximum use, of course, had not yet been made and was finally prevented by later-developing circumstances over which petitioner had no control."
>
> "* * * Its character as 'real property used in * * * trade or business' continues even after the planned use becomes impossible."

See also *Solomon Wright, Jr.* (1947) 9 T. C. 173.

It is axiomatic, as stated in *Goldberg* v. *C. I. R.*, 223 Fed. 2d. 705, that real property does not change the character bestowed upon it at the time of its original acquisition unless there is first established affirmative and significant acts to show a change of original intent:

> "If the property was originally acquired for rental purposes, it may nevertheless later be held for ordinary business sale to customers; and the converse may also be true. But the original purpose is important, for to counterbalance it there must be significant objective evidence of a change in that purpose."

In the instant case the record is devoid of any such "significant objective evidence" to show any change of original intent as to the particular property here involved.

It is important to note that the Tax Court and this Court have found facts showing that petitioner was active in real estate prior to the years involved and this is based not only upon his activities with respect to the Pennsylvania property, *but also similar activities as to many other properties.*

Conclusion

It is respectfully urged upon this Court that each of the cases cited herein warrants serious and thoughtful consideration. In each instance the Court has carefully and thoroughly considered a fundamental legal principle also involved in the instant case. Their views as to these basic principles and their application to not unlike facts is contrary to that of the Tax Court in this proceeding. Nor is it a complete or satisfactory rationalization of the patently erroneous conclusion of the Tax Court to hold that the issue is solely one of fact. While this may be true in part, it is nevertheless inescapable that, viewed in its entirety, the proceeding necessarily involves questions of both law and fact, and the ultimate conclusion of the Tax Court here complained of results from erroneous application of law as well as their failure to consider in proper context all of the pertinent facts of record.

In consideration of the above argument and authorities, and in order that substantial justice may be done, petitioner prays that this Court grant a rehearing of this cause, or, in the alternative, that this cause be remanded to the Tax Court with instruction to hear additional testimony by petitioner, or on his behalf, as herein prayed, and that this Court's decision and mandate be modified accordingly. Affidavit summarizing proposed additional evidence is attached hereto and made a part hereof by reference.

Respectfully submitted,

WILTON H. WALLACE,
HENRY F. LERCH,
Attorneys for Petitioner.

Supporting Affidavit of Petitioner

DISTRICT OF COLUMBIA, SS.:

Robert H. McNeill, being first duly sworn, deposes and says:

That he makes this affidavit because of his desire to clarify in detail facts with respect to his real estate activities in the sale of the property involved in this controversy in order that this Court may have more complete information as to his relation to said property in a business sense and in connection with his business activities in the sale thereof.

Affiant says that he has in his office a mass of detail information with respect to continued activities from 1924, when he took title personally, through 1946, and that had such evidence been submitted to the Tax Court it could not, in good conscience, have found as a fact or as a matter of law that petitioner was not holding the property at Altoona, Pennsylanvia, *at all times,* from the date of his purchase in 1924, until it was finally sold as property used in his trade or business.

Petitioner testified with respect to his efforts to sell this property, using his best recollection and exhibits available to him in the Court room, at a very brief hearing when the case was tried before the Tax Court, but not going into detail.

Petitioner has available and in his possession an accumulation of data, *over a period of 32 years,* as to his activities and now asks the Court for a remand so that he may be allowed to submit this voluminous documentary and oral evidence to the Tax Court, so that substantial justice may be done, as contemplated by all Courts of justice, and particularly by this Court.

Affiant says that if he is given opportunity so to do he will be able to show, by oral and documentary testimony,

that *from 1924 to 1946*, he persisted, through agents, attorneys and personally to do everything that could have been done reasonably or sensibly to sell said property, and in fact did negotiate through one Dr. Clarence J. Owens, an agent, for the sale of 300 acres of said property in 1936 to the City of Altoona for an airport—said sale only failed to be consummated because of the refusal of H. W. VanSciden, mortgagee, to release the property from his mortgage upon consummation of said sale to the City of Altoona, at the price of $10,000.00.

Affiant further states that if a remand, as above, is granted by this Court he can furnish the testimony of living witnesses who know of his personal activities in endeavoring to sell the property from 1924 through 1946, among whom will be Ashton Gardner, attorney-at-law, Hollidaysburg, Pennsylvania, and Robert C. Haberstroh, attorney-at-law, Kenneth Vaughn, Tax Commissioner, P. J. Morris, vice-president McVey Realtors, Harold E. March, attorney-at-law, and Frank Hunter, City Manager, all of the City of Altoona, Pennsylvania, and Hon. J. Banks Kurtz, former Congressman from Altoona, Pennsylvania, and Congressman James E. VanZandt of Pennsylvania, and has reason to believe that the documents he holds with respect to his efforts to dispose of the Altoona property for sale probably consists of hundreds of pages.

Petitioner makes this affidavit solely for the purpose of showing to this Court his continuing real estate activities as to this property up to the date his title actually expired in December, 1946.

Petitioner notes that this Court has found that his diligent efforts to sell the land in lots,

> "* * * may fairly be considered to have been in the real estate business at that time; but after this period the operation ceased."

Petitioner will show, if a remand is granted with directions to the Tax Court to hear additional testimony, that petitioner did not relax his efforts to dispose of the land, but continued them as above stated until he lost his equity of redemption in December, 1946.

If this Court so permits petitioner will testify and state that he purchased the property in 1924 with the intention and purpose to have it sold to anyone able to buy and *that he never changed this purpose at any time*, and that it was always on the market for sale in the City of Altoona and elsewhere until the final loss of title in 1946.

/s/ ROBERT H. MCNEILL.

SUBSCRIBED and SWORN TO before me this 26th day of February, 1958.

/s/ EDNA A. THOMAS,
NOTARY PUBLIC, D. C.

[SEAL]

Order Denying Petition for Rehearing

Filed and Entered March 17, 1958.

UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

No. 7527

ROBERT H. MCNEILL, *Petitioner*

versus

COMMISSIONER OF INTERNAL REVENUE, *Respondent*

The petition for rehearing of the appeal in this case or, in the alternative, for modification of the mandate to require the Tax Court to take further evidence has been read and considered and the Court is of the opinion that

the petition for reargument is without merit and that the appellant had full opportunity to present any evidence bearing on the merits of the case at the trial in the Tax Court.

It is therefore ordered that the petition be denied.

MORRIS A. SOPER
United States Circuit Judge

CLEMENT F. HAYNSWORTH, JR.
United States Circuit Judge

R. DORSEY WATKINS
United States District Judge

March 24, 1958, mandate issued and transmitted to the Clerk of the Tax Court of the United States.

March 24, 1958, record of original papers, and original exhibits returned to the Clerk of the Tax Court of the United States.

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INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	2
Argument	6
Conclusion	9
Appendix	10

CITATIONS

Cases:	
Chicago Title and Trust Co. v. *United States*, 209 F. 2d 773	7
Dillon v. *Commissioner*, 213 F. 2d 218	6
Dougherty v. *Commissioner*, 216 F. 2d 410	6
Home Co. v. *Commissioner*, 212 F. 2d 637	6
Morley v. *Commissioner*, 8 T. C. 904	7
Phipps v. *Commissioner*, 54 F. 2d 469	7
Smith v. *Dunn*, 224 F. 2d 353	6
Stockton Harbor Industrial Co. v. *Commissioner*, 216 F. 2d 638, certiorari denied, 349 U. S. 904	6
United States v. *Robinson*, 129 F. 2d 297	7
Statutes:	
Internal Revenue Code of 1939:	
Sec. 23(e) (26 U. S. C. 1952 ed., Sec. 23(e))	6
Sec. 23(g) (26 U. S. C. 1952 ed., Sec. 23(g))	6
Sec. 24(b) (26 U. S. C. 1952 ed., Sec. 24(b))	5
Sec. 117(a) (26 U. S. C. 1952 ed., Sec. 117(a))	5, 10
Sec. 117(d) (26 U. S. C. 1952 ed., Sec. 117(d))	6, 10
Internal Revenue Code of 1954, Sec. 1237 (26 U. S. C. 1952 ed., Supp. II, Sec. 1237)	8
72 Purdon's Pennsylvania Statutes Annotated (Permanent ed.), Sec. 6105.1	11

In the Supreme Court of the United States

OCTOBER TERM, 1958

No. 181

ROBERT H. MCNEILL, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 1a–15a)[1] are reported at 27 T. C. 899. The opinion of the Court of Appeals (R. 16a–21a) is reported at 251 F. 2d 863.

JURISDICTION

The judgment of the Court of Appeals was entered on January 11, 1958 (R. 21a), and the order denying petitioner's timely petition for rehearing (R. 22a–33a) was entered on March 17, 1958 (R. 33a–34a). The time for filing a petition for a writ of certiorari

[1] Record references are to petitioner's appendix to the petition for a writ of certiorari.

was extended to July 16, 1958, and this petition was filed on July 16, 1958. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254 (1).

QUESTION PRESENTED

Whether, on the facts of this case, the two courts below were correct in finding that petitioner was not in the real estate business during the years in issue, and that the property in question was not held primarily for sale to customers in the ordinary course of the taxpayer's trade or business at the time of its sale, with the consequence that the loss from the sale of such property was not an ordinary loss but a capital loss limited by Sections 23 (g) and 117 (d) (2) of the Internal Revenue Code of 1939, as amended.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 10–11.

STATEMENT

This case involves a deficiency in federal income tax for the year 1946.[2] The facts may be summarized as follows:

The property in question is the Wopsononock property, consisting of 834 acres, located near Altoona, Pennsylvania. Petitioner had advanced funds to a contractor who was constructing a railroad across the

[2] A deficiency for the year 1947 was also involved in the courts below. This deficiency was due to the Commissioner's disallowance of the claimed business bad debts. Both the Tax Court and the Court of Appeals sustained the Commissioner's determination that these debts were non-business bad debts. The petitioner does not attack here the courts' decisions regarding this bad debt question.

land and had guaranteed payment of a mortgage placed on the property by the contractor. When the mortgagor defaulted, petitioner acquired the property at a foreclosure sale, in November, 1924, to protect himself from loss on the mortgage. He intended to develop and subdivide the land, and sell the lots to the public either at auction or through separate sales transactions. Petitioner engaged experienced engineers to survey the property and prepare plats. He repeatedly advertised for the sale of the lots, and employed a prominent realtor in the community to solicit sales of the property, and made extensive efforts over a period of several years to sell the lots. All such efforts were completely unsuccessful. (R. 2a–3a, 17a.)

At a cost of $3,000, petitioner built a road through the forest to the top of the plateau where the lots held for sale were located. Attempts were made to construct an airport project within the area and the expenses in this connection amounted to $2,500. Petitioner also attempted to interest the State of Pennsylvania in developing a public park on the land. These attempts were unsuccessful. (R. 3a, 17a.)

In 1940, the Commissioners of Blair County, Pennsylvania, seized 458 acres (of the 834 acres) of the property because of nonpayment of realty taxes. Title to the property seized was retained by the Commissioners of Blair County for two and a half years while efforts were made by them to sell the property to a private owner after failing to dispose of the property to a public bidder for an amount equal to the unpaid taxes. After the property was seized for

nonpayment of realty taxes, petitioner continued his effort to sell all or part of the land since he retained a right of redemption. (R. 3a, 17a-18a.)

In 1942, title to the property was conveyed by the County Commissioners to the City of Altoona, Pennsylvania. The City of Altoona eventually offered to sell the property to petitioner and through his intervention, on December 5, 1946, title to the property was transferred from the City of Altoona directly to the Royal Village Corporation in consideration of $750, an amount less than the unpaid real estate taxes outstanding against the property. All of the capital stock of the Royal Village Corporation as of the date of sale, December 5, 1956, was held by petitioner and his family. (R. 3a–4a, 18a.)

At the time of the sale of the property to the Royal Village Corporation, petitioner's right of redemption expired. Petitioner thus lost his opportunity to recover his investment and, not having abandoned the property previously, he accepted this as the date of the realization of his loss. (R. 4a, 5a, 18a.)

While practicing law in Washington, D. C., petitioner participated in a number of real estate developments in Maryland, Virginia, District of Columbia and North Carolina. Occasionally, petitioner promoted and financed the construction of various buildings, including an office building in Washington, D. C. (R. 4a, 20a.) All of this activity occurred many years before the tax year in question. (R. 20a.) Petitioner has never held a real estate license. (R. 4a.)

Petitioner deducted $11,000 in his 1946 return as a loss arising from the abandonment of the property,

which he claimed was held by him primarily for sale to customers in the ordinary course of his trade or business. The Tax Court held that the loss was not deductible because it was prohibited by Section 24 (b) (1) (B) of the Internal Revenue Code of 1939 as having been incurred in a sale or exchange, directly or indirectly, between members of a family. (R. 4a, 6a, 12a.) The Tax Court also found that petitioner was not engaged in the real estate business during the years in issue, and that the property in question was not held by him primarily for sale to customers in the ordinary course of his trade or business at the time of its sale by the City of Altoona on December 5, 1946. (R. 5a, 6a, 7a.) The Court of Appeals reversed as to the applicability of Section 24 (b) (1) (B), but concluded (R. 19a–20) that the finding of the Tax Court, that petitioner was not engaged in the real estate business during the years in issue and that the property in question was not held by him primarily for sale to customers in the ordinary course of his business at the time of the tax sale in 1946, was not clearly erroneous. Therefore, the loss was a capital loss, deductible subject to the limitations of Section 117. A capital loss is deductible only to the extent of capital gains, plus the lesser of net income or $1,000.[3]

---

[3] Section 117 (a) (1) includes in the definition of capital assets all property held by the taxpayer except, among other things, property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. This Wopsonock property, therefore, was a capital asset unless it was held by petitioner primarily for sale to customers in the ordinary course of his trade or business during the years in issue.

Sections 23 (g) and 117 (d) (2). Losses incurred in a trade or business are fully deductible. Section 23 (e) (1).

ARGUMENT

1. The courts below were correct in finding that petitioner did not hold the property primarily for sale to customers in the ordinary course of his trade or business during the years in issue. That determination is essentially one of fact turning upon the particular circumstances of this case and presents no adequate ground for a writ of certiorari.

Whether property is held primarily for sale to customers in the ordinary course of business is, as the lower courts have uniformly recognized, a question of fact on which only clear error can justify reversal of the fact-finding tribunal. See e. g. *Stockton Harbor Industrial Co.* v. *Commissioner*, 216 F. 2d 638 (C. A. 9th), certiorari denied, 349 U. S. 904; *Smith* v. *Dunn*, 224 F. 2d 353 (C. A. 5th); *Dougherty* v. *Commissioner*, 216 F. 2d 110 (C. A. 6th); *Dillon* v. *Commissioner*, 213 F. 2d 218 (C. A. 8th); *Home Co.* v. *Commissioner*, 212 F. 2d 637 (C. A. 10th). As the Court of Appeals observed (R. 20a):

> During the years immediately following the acquisition of the Pennsylvania property in 1924, the taxpayer made diligent efforts to sell the land in lots and may fairly be considered to have been engaged in the real estate business at that time; but after this period the operation ceased. The subsequent attempts to dispose of the land for a public park or an airport also came to an unsuccessful end in the late 20s or early 30s. The testimony of

of the taxpayer as to what he did thereafter is confined to the general statement that he tried to dispose of the property and is entirely consistent with the conclusion of the Tax Court that the project was a failure and the Taxpayer did not operate it as a business in 1946, when the loss was claimed. The taxpayer supplements his testimony on this point by referring to numerous activities by him in the real estate field in various localities in or adjacent to Washington and in neighboring states, but most of these transactions took place prior to 1930 and all of them occurred many years before the tax year in question.

The lower courts' appraisal of the particular facts here affords no basis for establishing a conflict with other Courts of Appeals or with the Tax Court. See e. g. *Phipps* v. *Commissioner*, 54 F. 2d 469 (C. A. 2d); *Chicago Title and Trust Co.* v. *United States*, 209 F. 2d 773 (C. A. 7th); *Dillon* v. *Commissioner*, 213 F. 2d 218 (C. A. 8th); *United States* v. *Robinson*, 129 F. 2d 297 (C. A. 5th); *Smith* v. *Dunn*, *supra*; *Morley* v. *Commissioner*, 8 T. C. 904. Each of these decisions necessarily hinged upon the particular set of facts presented. While there have been occasional intimations of divergence in emphasis (see *United States* v. *Robinson*, *supra*, p. 300), the variety of factual circumstances presented makes it impossible to perceive a clear line of irreconcilable difference in the legal standards applied.

2. Contrary to petitioner's contention, the courts below did not disregard his "unimpeached" (Pet. 21) testimony. The Court of Appeals (R. 20a) con-

sidered the testimony when it stated that petitioner's efforts to sell the land in lots following the acquisition of the property in 1924 may fairly be considered as evidence that petitioner "engaged in the real estate business at that time; but after this period the operation ceased." (R. 20a.) The subsequent attempts to dispose of the land for a public park or an airport also came to an unsuccessful end in the late '20s or early '30s. The petitioner's testimony as to what he did thereafter is confined to "the general statement that he tried to dispose of the property and is entirely consistent with the conclusion of the Tax Court that the project was a failure and Taxpayer did not operate it as a business in 1946, when the loss was claimed." (R. 20a.) In other words, the petitioner has failed to carry his burden of proof by showing here that the property involved was held primarily for sale to customers and by showing that he was conducting a real estate business at the time the property was taken over in 1940.[4]

---

[4] It should be noted that Section 1237 of the Internal Revenue Code of 1954 formulates new and detailed rules to assist in determining whether and to what extent profit from sales of lots in a subdivision is to be treated as ordinary income or capital gain. Applicable to sales after December 31, 1953, this provision sharply diminishes the future importance of cases like the present one arising under the Internal Revenue Code of 1939.

CONCLUSION

The concurrent findings of both courts below are amply supported by the record and do not warrant further review. Accordingly, the petition for a writ of certiorari should be denied.

Respectfully submitted.

J. LEE RANKIN,
Solicitor General.

CHARLES K. RICE,
Assistant Attorney General.

A. F. PRESCOTT,
CHARLES B. E. FREEMAN,
Attorneys.

AUGUST 1958.

APPENDIX

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by Individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; * * *

* * * * *

(g) *Capital Losses.*—

(1) *Limitation.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117.

* * * * *

(26 U. S. C. 1952 ed., Sec. 23.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

(1) *Capital assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, * * *

* * * * *

(d) [As amended by Sec. 150 (e) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Limitation on Capital Losses.*—

* * * * *

(2) *Other taxpayers.*—In the case of a taxpayer, other than a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of the gains from such sales or exchanges, plus the net income of the taxpayer of $1,000, whichever is smaller. * * *

* * * * *

(26 U. S. C. 1952 ed., Sec. 117.)

72 Purdon's Pennsylvania Statutes Annotated (Permanent ed.):

SEC. 6105.1. *Right of redemption upon payment by installments*

In all cases where heretofore or hereafter real property shall have been or shall be purchased at any tax sale by any political subdivision, any person who was or is entitled under existing law to redeem such property shall have such right of redemption so long as the title thereto remains in said political subdivision upon the payment of the amount due thereon by installments in the manner hereinafter provided, whether or not the period during which the right of redemption existed shall have expired.

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IN THE

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No. 181

ROBERT H. McNEILL

v.

COMMISSIONER OF INTERNAL REVENUE

MEMORANDUM IN REPLY TO BRIEF FOR THE RESPONDENT IN OPPOSITION

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MEMORANDUM IN REPLY TO BRIEF FOR THE RESPONDENT IN OPPOSITION

The Petition for Certiorari was filed on July 16, 1958. Thereafter, on August 15, 1958 the Brief for the Respondent in Opposition was filed. The instant Memorandum is now respectfully submitted by petitioner for reply to respondent's brief.

ARGUMENT

The fallacy of respondent's position in this proceeding is clearly demonstrated by an analysis of his brief in opposition. By patently ignoring and side stepping the fundamental issues raised by the petition

herein, respondent in effect concedes his inability to answer them effectively.

1. It is the position of petitioner that the following facts found by the Tax Court can properly support no conclusion other than that the property was held by him primarily for the sale to customers.

* * * * * * * * *

"He desired to sell the lots to the public either at auction or through separate sales transactions. Petitioner engaged experienced engineers to survey the property and prepare plats of the land to be offered for sale.

At a cost of $3,000, McNeill built a road through the forest to the top of the plateau where the lots held for sale were located.

Petitioner repeatedly advertised for the sale of the lots. He employed a prominent realtor in the community to solicit sales of the property, and made extensive efforts over a period of several years to sell the lots. All such efforts were completely unsuccessful.

Attempts were made to construct an airport project within the area, and also to interest the State of Pennsylvania in developing a public park on the land, but without success. Petitioner's expenses in connection with his attempt to develop an airport on the land amounted to $2,500.

In 1940 the Commissioners of Blair County, Pennsylvania, seized 458 acres of the property in question because of nonpayment of realty taxes and retained title thereto for 2½ years, attempting meanwhile to sell it to a private owner after failing to dispose of the property to a public bidder for an amount equal to the unpaid taxes. During 1942 the property was conveyed by the County Commissioners to the City of Altoona, Pennsylvania. *After the acquisition of 458 acres of the*

Wopsononock tract by Blair County, and later by the City of Altoona, petitioner continued his efforts to sell all or part of the land since he retained a right of redemption therein." (App. 2a, 3a) (Emphasis Added)

* * * * * * * * *

"Moreover, his conduct in further attempting to sell the land after its seizure by Blair County and in offering to satisfy the mortgage outstanding against the property in May 1946 demonstrates his intention to retain control over it. Such conduct is clearly inconsistent with abandonment." (App. 6a)

* * * * * * * * *

To thereafter conclude that the property was not held primarily for sale is a non-sequitur, clearly erroneous and contrary to fundamental logic.

Respondent's primary argument is that the question here involved is one of fact and that the lower courts' appraisal of the particular facts afford no basis for establishing conflict with other courts of appeal or the Tax Court.

Respondent has not and, in fact, cannot reconcile the rationale of the courts below in the instant proceeding with *Albert Kruse*, (1957) 29 T.C. 463; *Walter G. Morley*, (1947) 8 T.C. 904; *Carter-Colton Cigar Co.*, (1947) 9 T.C. 219; *Solomon Wright, Jr.*, (1947) 9 T.C. 173, and *Julius Goodman*, (1939) 40 BTA 22, all supporting the view that the character bestowed upon real property at the time of its acquisition is thereafter retained unless subsequently changed by significant actions. Surely respondent does not here consider as controlling the fact that petitioner at age seventy (70), which he was during the years involved, was not as physically active as he had been as a young

man nearly a quarter of a century before when he originally acquired the property.

To argue as respondent does he not only must ignore the facts found by the court below but must also of necessity utterly disregard the fundamental principles so thoroughly established by the many cases cited by petitioner.

Petitioner respectfully submits that respondent has done nothing more than rely on broad generalities that are not here applicable. The inescapable fact is that here the courts below are wrong and this Court should not permit the overworked cliche that issues of this type are mere questions of fact to be used in such manner as to insulate an erroneous determination from review.

2. The courts below have definitely disregarded the uncontradicted testimony of an unimpeached witness. This simple fact is inescapable despite respondent's statement to the contrary.

Petitioner testified that the real estate owned by him was primarily for sale to customers during the years involved (App. 25a). There were absolutely no facts or even the slightest scintilla of evidence to the contrary. This testimony was entirely disregarded, however, and the Tax Court concluded that the properties were not held primarily for sale.

The primary purpose or intent for which a person holds real estate or any other asset is subjective and best known to that individual for the simple reason that a court cannot look into a person's mind. Petitioner's testimony as to his intentions with respect to the property here involved was neither inherently improbable nor contrary to any proven facts of record. Under these circumstances it cannot be disregarded. *Pennsylvania RR Co.* v. *Chamberlain,* (1933) 288 US

333; *Foran* v. *Commissioner,* (CA 5 1948) 165 F. 2d 705; *Wener* v. *Commissioner,* (CA 9, 1957) 242 F. 2d 938.

Nor should this Court overlook the fact that the Tax Court's determination, which the Court of Appeals considered binding upon it that the property here involved was not held primarily for sale to customers was no more than dictum on the part of the trial court for the reason that such a determination was unnecessary to its disposition of the issue before it.

CONCLUSION

Respondent attaches undue significance to the fact that each of the courts below concluded that the property here involved was not held primarily for sale to customers. Petitioner respectfully suggests that to urge denial of the petition for a writ of certiorari on this basis is merely to ask this Court to compound the errors committed below.

Nor is respondent's footnote reference to Section 1237 of the Internal Revenue Code of 1954 pertinent. In the first place, this section pertains to transactions of a different character than here involved; secondly, this particular section was enacted many years following the years here involved and it is therefore not pertinent and, third, and most important, even if the hypothesis of the respondent be correct the rights of the instant petitioner are those to be considered, and they should not be sacrificed merely because of a subse- they should not be sacrificed because of any non-applicable change in the law and its imaginary effect on future taxpayers.

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